This record is a partial extract of the original cable. The full text of the original cable is not available.

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STATE PLEASE PASS AIT/W AND USTR

STATE FOR EAP/RSP/TC, EAP/EP AND EB/IFD/OIA

USTR FOR SCOTT KI

USDOC FOR 4420/USFCS/OCEA/EAP/LDROKER
USDOC FOR 3132/USFCS/OIO/EAP/ADAVENPORT
TREASURY FOR OASIA/MOGHTADER
TREASURY PLEASE PASS TO OCC/AMCMAHON
TREASURY ALSO PASS TO FEDERAL RESERVE/BOARD OF
GOVERNORS, AND SAN FRANCISCO FRB/TERESA CURRAN

E.O. 12958: N/A
TAGS: EINV EFIN ECON TW
SUBJECT: Taiwan's Next Step in Chunghwa Telecom
Privatization mid-2005

SUMMARY

¶1. Taiwan Premier Frank Hsieh has revived Taiwan's stalled privatization plans by ordering the sale of another 17% of government equity in Chunghwa Telecom Company (CTC), Taiwan's largest telecomm firm. The planned transaction will reduce government ownership in CTC to below 50%. Revenue from the sale will make a one-time contribution be used to supplement bond issuances to help reduce the 2005 budget deficit. Underwriters, investment bankers, and most economists welcome the plan, but it is strongly opposed by Chunghwa's labor unions. END SUMMARY.

Privatization

¶2. Taiwan's accession to the WTO in 2002 brought with it a commitment to undertake privatization of its many state-owned enterprises. Starting in the late 1990s, Taiwan began the CTC privatization process by separating CTC from the Ministry of Transportation and Communications. The next planned stage, in 2001, failed as strong opposition from labor, coupled with support from Legislative Yuan (LY) members, stopped the planned public sale of a portion of government ownership of CTC. Revisiting the program in 2003, the government sold off just over 35% of its equity in CTC.

¶3. In early March 2005, Premier Frank Hsieh instructed the Ministry of Transportation and Communications (MOTC) to move to the next stage of privatization and sell an additional 17% of government equity by mid-2005. This would reduce government ownership from 64.89% to 47.89%, making CTC a private firm according to Taiwan's definition of "state-ownership." As a private company, CTC would no longer be subject to supervision by the Legislative Yuan (LY) and its chairman would no longer be required to report to the LY. However, CTC would, of course, still be under the control of Taiwan's telecom laws and regulations.

Largest Secondary Offering

¶4. The CTC sale could generate about US$3.4 billion (or NT$105 billion at the current exchange rate of NT$30.9 per US dollar) and would be the island's largest secondary share offering ever. Analysts expect Taiwan will follow up with further privatization efforts, including the sale of 40% ownership in Changhwa Commercial Bank. That bank deal is currently valued at US$2 billion and should be completed by the end of 2005 (septel).

Higher Share Price

¶5. CTC share prices reached a four-year high of NT$64.1 on March 10, a possible factor behind the Premier's decision to sell at this time. In addition, investors may be attracted by CTC's 2004 dividend yield of 7%, higher than prevailing interest rates 2% on bank deposits (This doesn't quite ring true to me. A foreign investor will evaluate against all other investment options -not just Taiwan domestic interest rates on bank deposits.) . CTC recorded NT$50 billion in profits in 2004. CTC's share price puts it at a price-earnings ratio of 12. China Airlines, another profitable state-owned enterprise, has a P/E ratio of 11. CTCLet's compare apples to apples, you cite the dividend yield above, what is China Airlines dividen yield and how about the

return on asset figure for both CTC and CAL? has 13 million fixed-line subscribers and more than eight million mobile customers among Taiwan's population of 23 million. CTC occupied 84% of Taiwan's telecom market in terms of 2004 sales.

Public Debt Buildup

¶6. The estimated revenue of NT$105 billion from selling 17% of CTC equity shares would cut the need to issue public bonds in 2005 by nearly 60% to NT$150 billion. Projections for outstanding public debt as of December 2005 would be reduced by 2.8% and outstanding debt as a share of GNP would decline one percentage point from 35.7% to 34.7%. According to Lin Shuen-yu, a senior specialist of the Budget Bureau, Taiwan's fiscal deficit in 2005 would reach NT$336 billion without the planned sale of CTC equity. If the sale does not materialize, Taiwan would finance the fiscal deficit by issuing NT$255 billion in public bonds and using NT$81 billion of the government's past cash savings.

Business Opportunities

¶7. The plan to sell CTC shares will provide investment bankers and underwriters a good commercial opportunity. The estimated underwriting fee of US$60 bmillion (How does Taiwan make money out of this deal if the fees to collect NT$105 billion are US$ 60 billion, well above the income to be generated?) will attract Goldman Sachs, Merrill Lynch and UBS Securities, which arranged the CTC equity sales of US$1.37 billion in 2003. Other contenders for underwriting include Morgan Stanley, Credit Swiss First Boston, Citigroup, Daiwa Securities, Nomura Securities, and Deutsche Bank.

Labor Opposition to Sale

¶8. CTC labor unions have opposed privatization and may try to block the planned sale. The LY has passed resolutions requiring that CTC resolve issues with the unions before any sale. Lee Ching-sung, Chief of the Privatization Task Force under the Council for Economic Planning and Development, told AIT/T that the planned sales could fail again if MOTC fails to persuade CTC employees to give up the monthly pension privilege that they are still entitled to even after CTC was split from the Directorate General of Telecommunications in the late 1990s. Ms. Peng Su-ling, a senior economist of the Chunghua Institution for Economic Research, told AIT/T that CTC house labor unions oppose privatization because CTC employees would lose their status as civil service employee, see a decline in wages, and face higher performance standards. However, Ms. Peng believed that privatization was in the interest of the entire economy due to increased competition and higher efficiency. We expect the government will proceed with sale of CTC equity in spite of labor opposition. I thought the budget bill in January cancelled the privatization plans. What has changed to make this privatization possible now? Can we assess whether this will really go through or not? Will labor opposition/political intrigue combine to kill the move?
PAAL